

TO: Files

CC: Audit Committee

FROM: Willkie Farr & Gallagher LLP

RE: Interview of George Loveland, October 19, 2005

DATED: October 27, 2005

On Wednesday, October 19, 2005, Michael Schachter and Sharon Blaskey, in Willkie Farr & Gallagher LLP's capacity as counsel to the Audit Committee, interviewed George Loveland at the City Administration Building ("CAB"), 202 C Street in San Diego, in a conference room on the third floor. Mr. Loveland was not represented by counsel. Also present at the interview was Omid Yazdi of KPMG.

The following memorandum reflects my thoughts, impressions and opinions regarding our meeting with George Loveland, and constitutes protected work product. It is not nor is it intended to be a transcript of the interview.

Warnings

Mr. Schachter began the interview by informing Mr. Loveland that Willkie Farr & Gallagher LLP is counsel to the Audit Committee for the City of San Diego (the "City"), and does not represent Mr. Loveland or any employee of the City individually. He stated that the City of San Diego retained the Audit Committee to conduct an investigation, in part to give KPMG confidence in the City's financial reporting. The Audit Committee may write a report that may be used by KPMG and governmental agencies, and therefore Mr. Schachter emphasized the importance of Mr. Loveland being accurate and truthful in his responses. Mr. Schachter also told Mr. Loveland that the communication was not a privileged one, but that we did ask that he keep it confidential. Mr. Loveland asked whether the privilege had been waived as to closed session, and Mr. Schachter confirmed that it has been, except to matters involving pending litigation. Mr. Schachter informed Mr. Loveland that the focus of the interview will be on issues pertaining to wastewater and the City's compliance with certain requirements.

Background

Mr. Loveland stated that he was a City employee for 38 years. He started working for the City in 1967, in his senior year at San Diego State. He subsequently became a full time City employee in the Fall of 1967. He spent most of his career working in the park and recreation departments, in varied positions, including: as a water department director, as a transportation director, as an acting Deputy City Manager on an interim basis a couple of times, as a permanent Deputy City Manager, as a Senior Deputy City Manager, and in a variety of other supervisory jobs in the earlier part of his career. Mr. Loveland retired in January (either 13 or

15), 2005, and officially left of the City's payroll in April 2005, when his accrued vacation time lapsed. At the time of his retirement, he was the Assistant City Manager, which was the number two position in the City Manager's Office. He was an operational head and reported to Lamont Ewell. Mr. Loveland took that position when Ewell became City Manager. Mr. Loveland held that last position for about a year. Prior to becoming Assistant City Manager, he was the Senior Deputy City Manager. He took on that role in roughly 2000. It was at that time that Ewell came on board as the Assistant City Manager, and Mr. Loveland then became the Senior Deputy. The Senior Deputy City Manager position was one that was created for Mr. Loveland, and in substance, his responsibilities did not change much from those in his previous position as Deputy City Manager, with responsibility for public works (including transportation, sewage, and other groups). The reason the special position was created for him was that he had been passed over for the job that Ewell got (apparently, as he was told, because Mr. Loveland was close to retirement). When serving as Deputy City Manager, Mr. Loveland "generally" reported to the Assistant City Manager, though he described the reporting structure as somewhat "loose." He described Uberuaga's style as not getting involved in the day to day level of detail, and he described McGrory as being "more hands on." He served twice as an Acting Deputy City Manager in the course of his career, once when Coleman Conrad was on sabbatical, and one other time as well. In between those times, he also served as Water Department Director. The City Manager's Office was structured to contain more than one Deputy City Manager. Mr. Loveland described that there are generally four, each with a different portfolio. As described above, for the majority of his time as Deputy City Manager, Mr. Loveland's portfolio primarily concerned "public works" (including MWWD), though there were times he had responsibility over other areas, for example, the library.

Wastewater Issues

Mr. Loveland was first shown and reviewed the following documents to refresh his recollection:

- Exhibit 1 (COS 2108), an August 8, 1997 memo from William Hanley to Coleman Conrad (cc: Mr. Loveland and others), re: "Implementation of Strength Based Billing"
- Exhibit 2 (COS 2036), a November 6, 1997 memo from Hanley to Deborah Van Wanseele (cc: Mr. Loveland and others), re: "A. Deputy Water Director, Services Division Memo of March 17, 1997" This was the period he was in the water dept.
- Exhibit 3 (COS 0319), an April 1, 1998 letter from Langworthy to McKinley (cc: Mr. Loveland and others)
- Exhibit 4 (COS 7340), an October 21, 1998 memo from Schlesinger to Distribution (including Mr. Loveland), re: "Regional Wastewater Disposal Agreement-Review by State Water Resources Control Board"
- Exhibit 5 (MWWD BH0891), an October 26, 1998 letter from Schlesinger to Zapotichny (cc: to Mr. Loveland and others), re: "Cost of Services Study for Municipal Wastewater Services"

- Exhibit 6 (MWWD –BH 0930), a November 12, 1998 email from Hanley to Mr. Loveland, Schlesinger, Hamilton, re: “Meeting with Kelco-Strength Based Billing”
- Exhibit 7 (MWWD - BH 0929), an email from George Loveland to Zapotyczny (Monsant), dated 11/20/98, re: “re: Strength Based Surcharge-Reply”
- Exhibit 8 (BH – 0892), a letter from Hanley to McKinley, cc: Mr. Loveland and others, dated November 24, 1998
- Exhibit 9 (MWWD 02350), a letter from McKinley to Hanley, cc: Mr. Loveland, dated Dec. 14, 1998, re: “Specific Problems with Wastewater Strength-Based Cost Allocation Factors”

Referring to Exhibit 1 (dated August 8, 1997), Mr. Loveland thinks he was the Water Department Director at the time the memo was written. The memo states, in part: “This memorandum responds to your request for an update and schedule for the implementation of strength based billing for sewer services. . .” He thinks he would have received this memo because the billing system for sewer was done by the water department and he would have been kept in the loop as to the billing issue. He stated that as of this time in 1997, he had “some” understanding as to how the sewer user rates were structured, but that he became more conversant in the issue later down the road. Generally, he said that he had been part of some discussion at various times as to issues surrounding the mechanics of billing and changes necessary in the billing software to implement rate changes. The memo references the subject of “strength based billing.” As to whether Mr. Loveland had an understanding in 1997 or 1998 that the sewer rate structure was not in compliance, Mr. Loveland responded that he was “not sure that he knew at that time,” but that he “certainly came to learn it at some point.” He thinks he became aware that they were out of compliance through conversations with Kahlie and Hanley. He generally recalls that these conversations had to do with the State Revolving Fund (“SRF”) loan program. He learned that, as a condition of the loan, the City had to comply with certain requirements. He said that over time, there was “quite a discussion” of how to and what to do to comply. He said the compliance issue segued into issues with Kelco and others, including the restaurant associations, as to what sewer rate formula should be used. Generally he recalls that there were two issues: (1) were the technical arguments correct about the way in which the strength of sewage must be measured, or were there other ways to measure it; and (2) were there ways to pretreat large users’ sewage, to lower their sewage strength and thereby cut their costs.

In response to whether Mr. Loveland recalled a time that the Participating Agencies’ (“PA’s”) contracts were revised to be compliant but that the City’s users were still not in compliance, Mr. Loveland confirmed that there was a period of time in which the PA’s had changed their rates while the City had not. It was during this time that he recalls going over the preceding two arguments. He does not recall how the decision was made that the PA’s would come into compliance but the City would not, and he does not think he was directly involved in that decision. His “anecdotal” understanding was that when the time arrived that the City considered implementing the compliant rate structure for the PA’s, the City’s retail customers got more specifically involved and got into the argument over the correct formula.

Mr. Schachter asked whether there were any particular elected officials that supported Kelco, and Loveland responded that there was a general position by Council not to change the rates in a way that would have a negative impact. Mr. Loveland understood that the Council was concerned with losing jobs and the waterfall effect of forcing industries out, and what would be the general economic impact of a rate change. Mr. Loveland recalls both informal and formal discussions at the Council about how to approach that sensitive issue. He recalls that staff eventually took the cost of service study ("COSS") forward to Council and that the response was that "there was quite a division" among Councilmembers, some of whom wanted to change rates, while others wanted to keep the structure as it was, and to explore whether there might be a less adverse solution "to the Kelcos of the world."

Mr. Loveland reviewed Exhibit 10 (COS 118), a memo dated October 6, 1999, from Mr. Loveland to the Mayor and City Council, re: "Water and Sewer Cost of Service Studies." He also reviewed Exhibit 11 (MWWD BH 950), the 1998 Pinnacle COSS. He has no specific recollection of the Pinnacle study, but based on reviewing the two documents, he said that it was "obviously one they [the City] did." It is consistent with his recollection that there was language in the study regarding a need for an organics component in the City's rate structure. Mr. Schachter asked Mr. Loveland, focusing on this October 1999 time period, why he communicated to City Council that "no changes are needed or recommended at this time," and who contributed to the decision to tell the Council that. Mr. Loveland stated that he recalls the reason they made this recommendation is connected with the sentence in Exhibit 10, "consistent with the requirements of Proposition 218." Generally, he recalls that the Council wanted to try to find a "business-friendly" way to deal with the sewer rates. The intention was not to be friendly to any particular business, but to businesses in general, because of the economic rationale to do so. He said that he had a great deal of difficulty and discussion between the City Attorney's Office (the "CAO") and the "water folks" as to what the requirements were.

He explained that the issue regarding Proposition 218 was that sewer rates were arguably not subject to Prop 218. The CAO had recommended that the City comply with portions of Prop 218 anyway, but there remained considerable disagreement about how to deal with it. He recalls that, as of this 1999 timeframe, most of the discussions concerned Prop 218 compliance rather than compliance with State requirements. As far as compliance with the State's requirements, Mr. Loveland recalls there being some initial difference of opinion as to whether or not the City had complied with the State's requirements, but at the end of the day, they agreed that, at a minimum, they probably were not in compliance with the interpretation of some of the State staff. As he was describing the two different arguments, Mr. Loveland acknowledged that he "gets confused" about which timeframe these things occurred. At some point he recalls spending a lot of time trying to determine whether there was any latitude in the State's requirements. During that time, he said, they were getting lobbied heavily by Kelco, the Chamber of Commerce, and others. Doug Sain was spearheading the effort of one of the groups, which efforts would involve proposing methodologies. Mr. Schachter corrected Mr. Loveland that the stakeholder's group to which Loveland was referring had actually occurred later than this 1999 time period on which we were focusing. Bringing Mr. Loveland's attention back to the memo (Exhibit 10), Mr. Schachter asked Mr. Loveland who he spoke with about it, and who made the decision that gave rise to the sending it. The only person Mr. Loveland could "say for sure" that he spoke with about it was Kahlie, since Kahlie had written the memo (as reflected by

the initials "DHK" under Mr. Loveland's signature). Though Kahlie wrote it, Mr. Loveland said it was "fair to say" that Mr. Loveland had directed him to. Mr. Loveland was aware that Kahlie's position was generally that there *were* changes that needed to be made to the rate structure, and Mr. Loveland acknowledged that the memo's language recommending that no changes were necessary would not have been Kahlie's "tendency."

Mr. Loveland, responding to why he would have directed Kahlie to make this recommendation, said that the memo would not have gone out without Mr. Loveland first discussing it with the City Manager (Uberuaga, at that time), and the City Attorney (by which Mr. Loveland said he did not mean Gwinn personally, but rather, a member of his staff). As to with whom he would have discussed the issue, he thinks Kelly Salt would have been one person, though he cannot specifically recall an exact conversation with her. To the best of his recollection, Mr. Loveland said he discussed the issue with Mike [Uberuaga], with Salt, and with Les Girard. They had conversations with most of the Council discussing how the Council wanted to deal with the compliance issue, and Mr. Loveland said that it was "very clear," that with the exception of one or two Councilmembers, for business reasons, Council did not want to change the rates unless they needed to do so. As to whether it was his decision to send the memo to the Mayor and City Council, Mr. Loveland said that he thought Council directed them to bring the study forward. He reaches that conclusion because he does not think they would have moved forward absent Council's direction. Mr. Loveland again cautioned, however, that his recollection may be "fuzzy" on time periods generally, and on what happened when. He said, "It all runs together." He elaborated that since he first became involved, "it was virtually the same argument all the time." He does not recall the specifics of what prompted him to send the memo, and though he does not recall, he said the decision to do so may have been his, but it would not typically be a decision that he would make alone. He thinks Salt may have participated in the discussion about whether to send it, but that she would not be part of the decision making process. He recalls very little of Les Girard's involvement but described that Les was always "the final arbiter" of the advice of the CAO, and was in the position of saying where the CAO would land on various issues. Mr. Loveland recalls general discussions with Uberuaga in which Uberuaga voiced concern with the rates and the Council's desire not to change them.

Mr. Schachter observed to Mr. Loveland that the "circumstances" of the memo were unusual, given that the study was dated May 1998, but the memo transmitting the study was dated October 1999. Mr. Loveland thought the delay in transmitting the COSS resulted from the City "internal[ly] vetting" the various issues: what they needed to do with respect to Prop 218, compliance with State requirements, and Council not wanting to change the rates if they didn't have to. Mr. Loveland does recall speaking with Council about these issues. He said that he tried to lay out to Council the various parameters of the issue and the points of disagreement about what needed to be done. He said he presented to the Councilmembers whether they were obligated to make certain changes or whether they had options. Mr. Loveland said that, at the end of the day, when it was presented to Council, "it was in the vein of, you don't have to do it and you'll comply with Prop 218." He said he is "fuzzy" on why the focus of the memo (Exhibit 10) was on Prop 218 rather than on the State requirement, but he offers by way of explanation that he "can only guess" that Prop 218 was the focus of the argument. Mr. Loveland said that, as of that time in 1999, he was "convinced" from the discussions they had, that "Council had the option to change the rates or not." In response to why he had that impression, he said that he arrived at it via discussions with the attorney, with Kahlie, and even with the consultants, about

whether it was so black and white that the Council had no options. As a follow-up to Mr. Loveland's statement, assuming the memo reflected Mr. Loveland's opinion at the time, Mr. Schachter attempted to clarify how he reached the conclusion that no changes were needed or recommended. Mr. Loveland said that his view came from conversations with his staff and the attorney's staff about what the options were. By "his staff," Mr. Loveland is referring to Kahlie and Hanley, with whom he spoke most often. While Mr. Loveland acknowledged that Kahlie would not have said that no changes were "needed or recommended," Mr. Loveland did state that he thinks he understood from Kahlie that they had "some flexibility." What he meant by "some flexibility" was that the COSS concluded that rates should be structured in a certain way, but that there was agreement that there were other ways to do it. Returning his focus to Exhibit 10, Mr. Loveland stated that he does not think he was referring to the State requirements, but rather, Prop 218. Mr. Loveland tried to reconcile the two and offer a viable distinction for purposes of his memo, and he ultimately could not come up with one. Mr. Loveland recalls that Hanley was "apolitical" on the issue and was just trying to get the facts. As for Mr. Loveland's own position on the issue, he said he does not know that he "had a position one way or another." Mr. Loveland does not know whether Hanley ever said that no changes were necessary. Of Uberuaga, Mr. Loveland characterized his "clear" position that he did not want to take a change to the Council if it was not necessary. Mr. Loveland recalls that the conclusion at the time was that the change was not required.

Mr. Schachter asked Mr. Loveland whether he knew, as of October 1999, that there was a requirement to include an organics component in the rate structure, and Mr. Loveland responded that he did know that, and that he also knew that there was not an organics component. He said that, perhaps he knew that "some" change was needed, but stated, "I don't know. I don't know." Mr. Loveland kept referring back to conversations he had had about whether compliance with Prop 218 was necessary, and he was having a hard time reconciling that recollection with what was in the report, and he said he "doesn't know why." When asked who on the City Council took the view that, unless absolutely necessary, there would be no changes, Mr. Loveland said that probably almost all of the Council members took that position. Again, he emphasized that he was "struggling with timeframes." He does not recall Coleman Conrad being involved in the decision not to implement the 1998 Pinnacle COSS.

Mr. Loveland was then shown and reviewed the following documents:

- Exhibit 12 (DK 09920), an email from Schlesinger to Mr. Loveland and Larry Gardner, dated October 19, 1999, re: "Water and Sewer Cost of Service Studies"
- Exhibit 13 (COS 5530), an email from Schlesinger to Zembrano, cc: Mr. Loveland and others, dated October 20, 1999, re: "re: a couple of questions"
- Exhibit 14 (COS 5529) is an email from Schlesinger to Mr. Loveland, dated 11/1/99, re: "Grand Jury Review of Sewer Rates"

Having reviewed the exhibits, Mr. Loveland said that he recalls the events generally, but not specifically. In general he recalls that there was a lot of "push and shove" about whether or not they would change the rates to charge more on the industrial side over the residential side. He has no recollection of a Kehoe press conference, nor does he recall that Exhibit 10, the transmittal of the 1998 COSS, had anything to do with Kehoe's staff finding out about the COSS. Loveland does not recall having any conversations with Kehoe regarding

sewer COSS's, but he does recall conversations with her regarding sewer rates, generally. His recollection is from conversations even before the COSS, in connection with a concern Kehoe had with rate increases causing residents to pay more while industry would pay less. However, he has no recollection of Exhibits 12-14 either generally or specifically. He said he does recall the sewer user rate compliance issues being discussed, but just not in connection with Kehoe.

Switching gears to the sewer revenue bonds, Mr. Loveland said that in general he had no role in preparing the bonds, but he did work on the capital program portion. Mr. Loveland looked at Exhibit 15 (COS 005874), the 1999 Sewer Revenue Bond Official Statement, at 5904 (entitled "wastewater system regulatory requirements"). Mr. Loveland does not think he reviewed this section before it went out. They broke up the bond offerings into various parts, and his part was the capital project part. He said he did not participate in any page turners on the offering. He has been in meetings with Paul Webber, but not meetings of that type. He said he never participated in any meetings with Webber in which Webber was informed that the City was not in compliance with sewer user rates. Nor did he ever attend any meetings with Webber where Webber was told that the State could demand immediate acceleration of the State Revolving Fund (SRF) loans. Mr. Loveland said that it is possible that he may have had a meeting about the single section in which he was involved, but he does not recall one, nor does he recall a larger all-hands meeting.

Mr. Loveland was then shown Exhibit 16 (no bates), an email from Kahlie to Frazier and Mr. Loveland, with a cc: to others, dated 10/27/99, re: "10/28 stakeholder's meeting cancelled." The email discusses that the meeting would not be necessary since "the Manager is not recommending any changes to the presently existing water/sewer rate structures." Mr. Loveland does not recall this email but does generally recall the issue. According to Mr. Loveland, Patty Krebs, referenced in the email, represented Kelco, Sony and Bio-Com, and these industries were concerned about a possible rate change. He said that the email reflected the "culmination of much of what had gone on at that time." Exhibit 17 (COS000005), is an email, with attachment, from Kahlie to Mr. Loveland, dated 12/3/99, re: "Meeting with Chris Kehoe Nov 2 Re Cost of Services Study - Forwarded." Neither the subject line nor the substance of the email (regarding various issues in connection with a stakeholder's group and the COSS) refresh Loveland's recollection about a meeting with Kehoe and Uberuaga. He does not recall Uberuaga committing to Kehoe to update the study (as referenced in the email), but he does recall that Uberuaga told Mr. Loveland they would do an update. At COS 6 (the attachment to Exhibit 17), entitled "Discussion Outline: Sewer Cost of Service Study Conclusions - November 1, 1999," Mr. Loveland does not recall the document nor whether it related to a meeting with Kehoe. Exhibit 18 (DK9922), is a document entitled, "Sewer/Water Cost of Service Study," which Mr. Loveland does not recall ever having seen. Though the document states that, "George Loveland personally talked to Councilmember Kehoe," Mr. Loveland does not recall doing it.

Mr. Loveland was then shown and reviewed the following documents:

- Exhibit 19 (no bates), the Black & Veatch study dated November 30, 2001 and labeled "draft"
- Exhibit 20 (COS 000026), an email from Kahlie to Mr. Loveland dated 1/7/02, re: "Sewer 218 Closed Session Issue"

- Exhibit 21 (MWWD-BH0287), a 1/15/02 letter to Kahlie from Black & Veatch, attaching the Black & Veatch study (that no longer has a draft stamp)
- Exhibit 22 (no bates), a "closed session report" dated 1/29/02, listing Mr. Loveland as an attendee at that closed session

He recalls that, in substance, the Black & Veatch study reached "pretty much the same" conclusions as the 1998 study. He said he remembered two things from the January 2002 closed session: (1) the direction they got at the end, not to bring back the issue to the Council until the attorney decided what the City was required to do, and (2) there was considerable debate among Council as to what to do with it. Mr. Schachter asked Mr. Loveland to describe the closed session with "as much detail as possible." Mr. Loveland said that he recalls Frye arguing for doing something immediately. He said that Mayor Murphy argued against it, as did the others. He said that Frye and Mayor Murphy, as he recalls, were the two principal speakers, and that there was very little support for Frye's position. He does not recall a presentation to the Council, but he acknowledged that there must have been, and he does not know whether it was made by staff or by an attorney. Mr. Loveland does not recall if Salt or Kahlie were present at the closed session, and does not recall Kahlie making a presentation. He posited that either manager or attorney staff could have made a presentation, or perhaps there was no presentation because enough discussion had already taken place. He recalled that, specifically, Frye was in favor of going forward with the recommended changes. The Mayor's rationale for not wanting to go forward with the proposed changes was basically that the Mayor did not believe they were required to do it, and there was an economic reason not to do it (specifically, the vitality of the business community). Mr. Loveland does not recall Madaffer making the comment, "Let 'em sue us," but Mr. Loveland did say he could imagine him saying it because it sounds like a comment he would make. As Mr. Loveland described, "there were passions on both sides of it," but he would not necessarily characterize the discussions as "hostile or heated." Mr. Schachter asked what the argument was against changing rates in light of the second outside consultant saying that they needed to be, and Mr. Loveland said that he "can't articulate it." Going into closed session, his position was that the rates needed to be changed, and that is what they recommended. He thinks that he, Kahlie, and maybe Schlesinger, spoke to Councilmembers in individual meetings, and that he perceived that Frye was very much in favor of the change, but some others were not. Frye felt that the COSS should be transmitted, and she pushed to that end in both public and private sessions.

He thinks the rationale of those against the change had to do with the "general economic vitality" argument, essentially that if there were a rate increase, it would make it untenable for businesses to conduct business in San Diego. Mr. Loveland said that both he and Kahlie told the Councilmembers that the consequences of not complying with the rate structure would be that the State could recall the loans. He does not recall any discussions about a need to disclose the non-compliance to the general public. While Mr. Loveland said he knew that the MWWD published annual financials, he said he had no role in preparing them (that was for the Auditor), and he did not review them before they went out. He said he never participated in discussions about whether the non-compliance needed to be disclosed, and that he personally never considered whether it was a disclosure issue.

Exhibit 23 (CSD -MAI 5359) is a memo from Richard Mendes to Councilmember Frye, cc: Mayor & Councilmembers, City Manager, Assistant City Manager, Senior Deputy City Manager, and Kahlie, dated April 18, 2002, re: "Cost-of-Service Reports." Mr. Loveland does not recall Frye requesting the 1998 COSS studies, nor does he recall receiving this memo. He does not know why Mendes was sending Frye the studies, except by looking at what the memo itself says, that she asked for it. Exhibit 25 (SP_SEC_SC002382) is a Black & Veatch study dated May 2002 with the word "Draft" hand-stamped on each page. Exhibit 25 (no bates) is a memo from P. Lamont Ewell to the Mayor & City Council (on which Mr. Loveland does not appear to be copied), dated November 22, 2002. Exhibit 24 appears to be transmitting the May 2002 Black & Veatch study (Exhibit 24). He does not know why the memo would have transmitted the study to City Council at that time, and offered as a possible explanation for the delay that he recalls there was an issue with the study initially, and in response, Black & Veatch revised a few things. Mr. Loveland did not know the timeframe of those revisions. He also offered that he was surprised that Ewell (rather than he) signed the memo transmitting the study, and wondered whether he may have been on vacation at the time, since it is the kind of thing that would normally come from him.

Exhibit 26 (no bates) is an email from Kahlie to Ryan, Mr. Loveland and others, dated 11/13/02, re: "revision #2 to COS Briefing document," with a document attached, entitled "Salient Points: Sewer Cost of Service Compliance Issue, November 13, 2002." Mr. Loveland does not recall receiving this email from Kahlie, nor does he recall the attached document or why it may have been prepared. He does not recall that the issue was put on and then taken off the closed session agenda in November, 2002, and does not recall why this issue was not taken up or acted on by City Council. As to whether he had any conversations with anyone about the issue during this time period, he does recall putting the issue before John Kern, and the Mayor's Rules Committee Consultant (whose name Mr. Loveland could not recall). He does not recall if anyone else was present for those conversations, but he does recall saying that the attorney had opined and that the issue had to "go back on." He does not recall what happened next or why the issue was not put back on.

Exhibit 27 (COS 3553 -58), is a memo from Vattimo and Salt to Mayor and City Council regarding compliance with the State's requirements. Mr. Loveland does not have a specific recollection of the memo, but he does recall knowing that the CAO had made the decision that the City needed to implement the new sewer rate. He does not recall who told him that, and he could have learned it from the memo itself. Mr. Loveland said he could not offer any explanation as to why the rates were not changed throughout 2002 and 2003, given that the CAO had issued its opinion, because by then, Mendes had been brought in and was dealing with the issue more on a day to day basis.

Concerning a few general issues about Kelco: Mr. Loveland never heard of any discussions about anyone in government receiving anything of value from Kelco, or from anyone acting on Kelco's behalf. Mr. Loveland never received anything of value from Kelco while at the City, but he acknowledged that since he has left the City he did go to dinner one time with Sain and some other individuals from the water department, in connection with Sain's lobbying for something having to do with the water department. Individuals may have gotten campaign contributions from Kelco, but Mr. Loveland said he would not know that since he did not pay attention to contributions.

Regarding the 2003 sewer revenue bond issuance, he recalls that the City was issuing the 2003 sewer revenue bond, and that his role in it was the same role he described that he had in connection with the 1999 offering. In connection with that offering, he did not have any discussions with Paul Webber or anyone else about disclosing the City's continuing non-compliance. He said that he did not give any thought to the issue himself, and that they were "compartmentalized" in that regard. Mr. Loveland said that he did not have any role in reviewing or preparing the wastewater disclosure made in the annual financials in March 2004, but that he was aware of it. He thinks that he learned from Pat Frazier that they had discovered that "this" (apparently, the non-compliance) was something that should have been disclosed, and so they made the correction. He surmises that it was either Frazier or Webber that made the decision that the non-compliance needed to be disclosed. He did not have any conversations with anyone in March 2004 about whether Webber had been aware of the City's non-compliance before the time that the decision was made to do the disclosure. Nor did he have any conversations with anyone about whose fault it was that the non-compliance had not been disclosed to the markets before March 2004. He does not recall having any discussions with Kahlie about whether Kahlie had disclosed to Webber the City's lack of compliance, and he never heard, from any source, that Webber was saying that the compliance information was kept from him.

Mr. Schachter then concluded the interview by asking Mr. Loveland if there was anything else to bring to our attention. Mr. Loveland summarized his views on the wastewater history of non-compliance: he said that his experience with it was that "it was a long expanding period of back and forth over how to comply and what was required." They were looking into whether there were policy options, and if so, which policy would be appropriate for the City Council to adopt. Mr. Loveland said, "They struggled with that for a long time." Mr. Schachter responded that it was not clear from the documents what the explanation is for why nothing was changed, despite the multiple cost of service studies, and Mr. Loveland responded that there was a "general reluctance" by the Council to change the rate structure, and that they went back and forth with that over time. He said that he knows of nothing where someone tried to "not reveal information" or to "withhold information."

Omid Yazdi asked what happened to change Mr. Loveland's mind, between the time he wrote his 1999 memo saying that no rate changes were necessary, and the closed session when he said he did think they were necessary? Mr. Loveland said that the stakeholders group got involved with the process, and there were conversations with the State as a result, which led to a "back and forth with the State, far too many times." He said that he ultimately arrived at the conclusion, and does not know of anyone in the staff that did not also reach that conclusion, that the rates needed to be changed. This was in part a response to feedback they were getting from the State. Specifically, he said that it was the process of going through these steps that changed his mind, but that it took some time to get it "worked out." No specific point in time stands out as the turning point that caused him to change his mind.

WF&G